

Message Text

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14

ACTION NEA-12

INFO OCT-01 ISO-00 SPC-03 AID-20 EB-11 NSC-10 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 CIAE-00

COME-00 FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12 LAB-06

SIL-01 L-03 H-03 PA-04 PRS-01 USIA-15 AGR-20 DRC-01

/176 W

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P R 031139Z JAN 74

FM AMEMBASSY ISLAMABAD

TO SECSTATE WASHDC PRIORITY 2695

INFO AMEMBASSY KABUL

AMCONSUL KARACHI

AMCONSUL LAHORE

AMEMBASSY NEW DELHI

AMEMBASSY TEHRAN

AMCONSUL PESHAWAR UNN

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E.O. 11652: N/A

TAGS: EFIN, EIND, PK

SUBJECT: COMMENTS ON GOP NATIONALIZATION OF DOMESTICALLY
OWNED BANKS

REF: (A) ISLAMABAD 0001; (B) ISLAMABAD 0004

SUMMARY. GOP NATIONALIZATION DOMESTICALLY OWNED BANKS
NOT UNEXPECTED BUT TIMING WAS A SURPRISE. NATIONALIZA-
TION POLITICALLY POPULAR BUT EXPECTED TO FURTHER DEPRESS
CLIMATE FOR DOMESTIC PRIVATE INVESTMENT AND TO AGGRAVATE
EXISTING INFLATIONARY TREND IN ECONOMY. END SUMMARY.

1. AS MENTIONED REF A, BANK NATIONALIZATION, LONG
RUMORED, WAS NO SURPRISE GIVEN UNEQUIVOCAL PPP/MANIFESTO
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ON SUBJECT AND RECENT NATIONALIZATION MEASURES SUCH AS DOMESTICALLY

OWNEDVEGETABLE GHEE INDUSTRY AND RICE AND COTTON EXPORT TRADE. NEVERTHELESS, CONGENS KARACHI AND LAHORE (CONTRIBUTIONS FROM BOTH INCLUDED HEREIN) REPORT TIMING WAS SURPRISE TO BUSINESS SECTOR. ONLY AFTERNOON BEFORE EVENT MIN FINANCE MUBASHIR HASAN HAD BEEN ENGAGED IN 4-HOUR SESSION WITH LEADING MEMBERS OF BUSINESS COMMUNITY TOPPED OFF BY TEN MINUTE APPEARANCE OF PRIME MINISTER OSTENSIBLE PURPOSE OF WHICH WAS TO INSTILL FURTHER CONFIDENCE IN PRIVATE BUSINESS SECTOR.

2. IMMEDIATE FINANCIAL EFFECT TAKEOVER HAS BEEN MASSIVE DEPOSIT WITHDRAWALS FROM TAKEN-OVER BANKS, WHERE SEVERAL RELIABLE OBSERVERS, INCLUDING HEAD ONE US BANK, ESTIMATE DEPOSITS UNDER FICTITIOUS OR COVER NAMES TO HAVE BEEN AS HIGH AS 30-40 PERCENT OF TOTAL DEPOSITS. ONE US BANKER CONFIRMED KARACHI STAR REPORT OF JANUARY 2 CONCERNING MASSIVE WITHDRAWAL FROM HIS LAHORE BANK. (JANUARY 3 PRESS ANNOUNCEMENT INDICATES STAR BANNED FOR TWO MONTHS.) UNDER CIRCUMSTANCES PRESS REPORTS OF WITHDRAWALS TOTALING UP TO OR OVER RS. 200 MILLION DO NOT APPEAR EXCESSIVE. SHARP RISE IN GOLD PRICES TO RS. 520 (US\$52) PER TOLA (\$139/TROY OZ.) FOLLOWING BANK TAKEOVER IS INDICATION NEAR DESPERATE EFFORTS OF BLACK OR GRAY MONEY HOLDERS TO SWITCH OUT OF ACCOUNTS UNDER FICTITIOUS NAMES AND INTO GOLD OR COMMODITIES. GOP SPOKESMEN, HOWEVER, CLAIM THAT NORMAL BANKING CONFIDENTIALITY WILL BE MAINTAINED UNDER NEW BANKING REGIME.

3. BANK NATIONALIZATION MAY HAVE SHORT RUN POLITICAL ADVANTAGES AS IT IS GENERALLY POPULAR. NEVERTHELESS, NATIONALIZATION CAN ONLY BE EXPECTED TO FURTHER SHAKEN CONFIDENCE OF DOMESTIC INVESTORS AND RESULT IN RUMORS OF ADDITIONAL NATIONALIZATION MEASURES, PARTICULARLY IN IMPORTANT TEXTILE SECTOR. THUS, BANK NATIONALIZATION SHOULD ADVERSELY AFFECT NEW PRIVATE INVESTMENT AND COULD STIMULATE FLIGHT CAPITAL.

4. TO THE EXTENT THAT BANK NATIONALIZATION PROMPTS SHIFTS FROM CASH AND DEPOSITS TO REAL ASSETS, ALREADY SIGNIFICANT INFLATION (30 PERCENT IN 12 MONTHS) WILL BE LIMITED OFFICIAL USE

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ACCELERATED.

5. STATEMENTS OF GOP OFFICIALS THAT BANK NATIONALIZATION WILL RESULT IN GREATER CREDIT TO SMALL BUSINESSMEN AND AGRICULTURAL SECTOR CAN BE EXPECTED TO FUEL REQUESTS FOR ADDITIONAL CREDITS TO THESE GROUPS. HOWEVER, EXPANSION OF CREDIT IS AT VARIANCE WITH GOP-IMF STANDBY AGREEMENT AND WITH CURRENT TIGHT MONETARY POLICY

PROMPTED BY NEED TO COMBAT INFLATION. THUS ADDITIONAL CREDITS TO NEW BUSINESSES CAN ONLY BE ACCOMMODATED WITHIN CREDIT CEILINGS AT EXPENSE OF TRADITIONAL BORROWERS, LARGE FARMERS AND INDUSTRIALISTS, AND IMPORT-EXPORT SECTOR. A SIGNIFICANT CONTRACTION IN CREDIT TO THESE ESTABLISHED GROUPS COULD BE EXPECTED TO RESULT IN DECREASED PRODUCTION. IN ADDITION, RELATIONSHIPS BETWEEN BANKERS AND POTENTIAL BORROWERS WILL CONTINUE TO BE MAJOR LOAN CRITERIA, ALTHOUGH A MORE POLITICAL TONE CAN BE EXPECTED.

6. NATIONALIZATION ORDINANCE PROVIDES FOR PAYMENT OF COMPENSATION TO SHAREHOLDERS BUT DOES NOT SPECIFY MANNER OF PAYMENT. REPORTEDLY COMPENSATION IS TO BE IN FORM OF NEGOTIABLE BONDS BEARING INTEREST AT TWO PERCENTAGE POINTS ABOVE BANK RATE. THIS METHOD OF COMPENSATION HAS DRAWN ONLY SIGNIFICANT PRESS CRITICISM, ON GROUNDS THAT SMALL SHAREHOLDERS SHOULD BE COMPENSATED IN CASH. BYROADE

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